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### **DoD Issues In-Sourcing Guidance**

By Philip J. Davis and Daniel I. Nylén

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On May 28, 2009, in response to announcements by President Obama and Secretary of Defense Gates that the government would scale back the role of contractors in providing support services, William J. Lynn, the Deputy Secretary of Defense, issued a memorandum entitled "In-sourcing Contracted Services - Implementation Guidance" (Guidance). [1] The Guidance, which applies to all of the Department of Defense (DoD), implements the Congressional direction in the Fiscal Year 2008 National Defense Authorization Act that DoD give special consideration to in-sourcing a variety of different functions. [2] The mindset of the Guidance is indicated by statements that "[i]n-sourcing is a high priority of the Secretary of Defense" and "a Department imperative." Deputy Secretary Lynn thus directs DoD components to "review all contractual services for possible in-sourcing" and sets a deadline of July 31, 2009, for submission of in-sourcing plans. Guidance p.1, ¶ 1.2.

This alert reviews the analytical process or "decision tree" set forth in the Guidance by which DoD components are to evaluate contracted services for in-house performance by DoD civilian employees. The Guidance does not direct that any specific function be brought in-house.

The first step in the process is to determine whether the function is a "valid and enduring mission requirement." Id. ¶ 4.2.1. If the activity qualifies as an enduring function, the Guidance identifies a series of sequential analytical steps that govern the component's evaluation of the function and the determination whether the function belongs to one of two categories:

- (i) Those functions that "must" be in-sourced based on their characteristics (Must Transition Category) and
- (ii) Those functions that should be in-sourced but require "special consideration" primarily on the basis of human resources and cost issues (Special Consideration Category).

The Must Transition Category is for those functions that, due to their nature, should be performed by the government and generally "must be in-sourced as expeditiously as possible" to DoD civilian employees. To determine whether a function belongs in this Category, the agency must evaluate seriatim whether or not the function is (i) inherently governmental, (ii) exempt from private sector performance, (iii) an unauthorized personal service, or (iv) evidences problems with contract administration. See id. ¶¶ 4.2.2 - 4.2.5. The first three functions "must" be transitioned in-house to DoD; the fourth function "may" be in-sourced.

Any functions that are not in the Must Transition Category must nonetheless be evaluated to determine if they are in the Special Consideration Category. See id. ¶ 4.2.6; 10 U.S.C. § 2463(b) (mandating that special consideration be given to using DoD civilian employees for functions that are new or meet any of four criteria). The four functions for special consideration are (i) functions performed by DoD employees within 10 years, (ii) functions closely associated with inherently governmental functions, (iii) functions under contracts awarded on a non-competitive basis, and (iv) functions on contracts that have been performed poorly. See id. ¶ 4.2.6.

If a function is in this Special Consideration Category, the Guidance prescribes a further two-part test to determine if that activity should be transferred to DoD civilian employees. First, DoD must evaluate "whether there are any legal, regulatory, or procedural impediments to hiring DoD civilian employees to perform the work." Id. ¶ 5.2.1. This assessment includes a variety of factors, including evaluating any hiring and office space limitations. Id. Second, if DoD determines that there are no such impediments to DoD civilian employee performance, then a "cost analysis" must be conducted "to determine whether DoD civilian employees or the private sector would be the most cost effective provider" of the service. Id. ¶ 5.2.2. The Guidance suggests that these services "must" be in-sourced "if a cost analysis shows that DoD civilian employees would perform the work more cost effectively than the private sector contractor." Id. ¶ 4.2.6. DoD has not yet issued guidance for this cost analysis.

If a contractor service does not fall within either of these two categories, there is no compulsion, at least under the Guidance, to in-source the function to DoD. The attached flow chart, taken from the Guidance, illustrates the step-by-step process. Each step in the process, especially whether or not a function is inherently governmental or closely associated with an inherently governmental function, can require a detailed analysis and may be open to subjective judgments. If a contractor believes that its services may be subject to in-sourcing under the Guidance analysis, the contractor should consider developing legal and policy arguments explaining why their functions do not fit within the various categories and why it is in the best interest of the government that their activities not be in-sourced, and provide such analysis to the DoD component undertaking the review.

Wiley Rein has analyzed this DoD policy and can provide advice on legal and policy arguments for maintaining functions in the private sector.

[1] Memorandum from the Deputy Sec'y of Def. to the Secretaries of the Military Dept., et al. (May 28, 2009) (available at: <http://www.defenselink.mil/prhome/pi.html> under Manpower Policy Memorandum) (Guidance).

[2] The FY08 NDAA § 324 contained language mandating that special consideration be given to in-sourcing specific categories of functions. The section also contains direction for DoD to develop guidance to consider in-sourcing and prohibits the use of OMB Circular A-76 competitions in certain situations. This section is codified at 10 U.S.C. § 2463.

For more information, please contact Philip J. Davis at 202.719.7044 or [pdavis@wileyrein.com](mailto:pdavis@wileyrein.com) and Daniel I. Nylén at 202.719.7190 or [dnylen@wileyrein.com](mailto:dnylen@wileyrein.com).